No. 95-559

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

DOCTOR'S ASSOCIATES, INC. and NICK LOMBARDI,
Petitioners,

v.

PAUL CASAROTTO and PAMELA CASAROTTO,
Respondents.

On Writ of Certiorari to the Supreme Court of Montana

BRIEF AMICUS CURIAE FOR THE AMERICAN COUNCIL OF LIFE INSURANCE IN SUPPORT OF THE PETITIONERS

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QUESTION PRESENTED

Whether state laws that condition the enforceability of arbitration provisions upon standards not applicable to other kinds of contractual provisions are preempted by Section 2 of the Federal Arbitration Act.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

Cases

Statutes

TABLE OF AUTHORITIES—Continued

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INTEREST OF THE AMICUS

The American Council of Life Insurance ("ACLI") is the largest life insurance trade association in the United States, representing the interests of more than 600 member life insurance companies. These companies currently underwrite 90.9 percent of the life insurance in force in legal reserve life insurance companies in the United States.

Ensuring that states are not permitted to disfavor arbitration agreements, in violation of the Federal Arbitration Act, is a matter of vital importance to ACLI's members. First, these companies employ approximately 250,000 insurance sales representatives who have registered with the National Association of Securities Dealers ("NASD") to sell securities and, in conjunction with that registration,

have agreed to arbitrate all disputes with their insurer-employers. Second, a growing number of ACLI's members now use binding arbitration clauses in certain group annuity contracts, group health policies, and individual life insurance policies. Because of its genuine interest in promoting enforcement of arbitration agreements, therefore, ACLI submits this brief in order to provide the Court with the views of the life insurance industry on the important question presented by this case.[1] ACLI has previously filed *amicus* briefs in this Court on issues pertaining to the interpretation and enforcement of the Federal Arbitration Act. *See Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834 (1995).

STATUTORY PROVISIONS INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2 (1994), provides:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Mont. Code Ann. § 27-5-114(4) (1995) provides:

> Notice that a contract is subject to arbitration pursuant to this chapter shall be typed in underlined capital letters on the first page of the contract; and unless such notice is displayed thereon, the contract may not be subject to arbitration.

[1] Counsel for both the Petitioners and the Respondents have consented to the filing of this brief. Their consents are on file with the Clerk.

STATEMENT

1. Because Petitioners set the facts forth fully in their brief, ACLI only summarizes the facts here. On April 25, 1988, respondent Paul Casarotto ("Casarotto") entered into a franchise agreement with petitioner Doctor's Associates, Inc. ("DAI") to open a Subway Sandwich Shop in Montana. Appendix to Petition for Certiorari ("Pet. App."), at 12a-13a.[2] The franchise agreement included an arbitration provision that provided that "[a]ny controversy or claim arising out of or relating to this contract or the breach thereof shall be settled by Arbitration . . . ." Pet. App. 13a.

2. Casarotto subsequently filed suit against both DAI and Lombardi, as well as other defendants, in the Montana Eighth Judicial District Court, Cascade County ("the trial court"). In his amended complaint, he alleged that he had entered into the franchise agreement and opened his shop at a less desirable location in reliance upon false representations by DAI and Lombardi that he would have the exclusive right to open a shop at a more desirable location when that location became available. Pet. App. 13a; Petition for Certiorari ("Pet."), at 5. He also alleged that DAI and Lombardi had interfered with efforts to sell his store. Pet. 5. On the basis of these allegations, he asserted claims for breach of contract, various torts, and violation of the Montana Consumer Protection Act. Pet. App. 13a; Pet. 6.

DAI and Lombardi moved to dismiss or stay the lawsuit pending arbitration, pursuant to the arbitration provision in the franchise agreement. The trial court granted the motion to stay, holding that the franchise agreement

[2] Petitioner Nick Lombardi is DAI's development agent in Montana. Pet. App. 12a. Respondent Pamela Casarotto is Casarotto's wife. The opinions of the courts below treated both Casarottos alike, although in fact only Paul Casarotto is asserting claims against DAI and Lombardi. Petition for Certiorari ("Pet."), at 5 n.4.

concerned interstate commerce, that Casarotto's claims against DAI and Lombardi "ar[o]se out of and relate[d] to the franchise agreement," and that DAI had properly demanded arbitration. Pet. App. 49a-50a.[a]

3. The Montana Supreme Court reversed the trial court's order. Its sole reason for doing so was that the franchise agreement did not comply with Mont. Code Ann. § 27-5-114(4), which provides that arbitration provisions are unenforceable unless the contracts containing them contain "[n]otice that [the] contract is subject to arbitration . . . typed in underlined capital letters on the first page of the contract . . . ." Pet. App. 27a.

4. DAI and Lombardi appealed the Montana Supreme Court's decision to this Court, which vacated the judgment and remanded for further consideration in light of *Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834 (1995). *See Doctor's Associates, Inc. v. Casarotto*, 115 S. Ct. 2552 (1995).

5. Notwithstanding the order to reconsider its earlier decision in light of *Terminix*, the Montana Supreme Court summarily reaffirmed and reinstated its original decision in the case, stating that "we can find nothing in the [*Terminix*] decision which relates to the issues presented to the Court in this case." Pet. App. 6a-7a.

SUMMARY OF ARGUMENT

I. Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2 ("Section 2"), provides that written agreements to arbitrate, when contained in contracts evidencing interstate commerce, must be enforced unless they are invalid on the basis of state law principles (such as duress) that are generally applicable to all contracts. Therefore, if a state conditions the enforcement of arbitration agreements

[a] These findings were not disturbed on appeal. *See* Pet. App. 6a (Montana Supreme Court assumed that there was a sufficient nexus with interstate commerce and that the Federal Arbitration Act was applicable).

upon compliance with requirements that the state does not obligate other kinds of agreements to meet, the additional requirements conflict with Section 2. The Montana notice statute at issue in this case makes arbitration provisions unenforceable unless they satisfy requirements that Montana law does not require other kinds of contractual provisions to meet. Consequently, the Montana notice statute conflicts with Section 2 and is preempted by it.

II. If states like Montana were permitted to impose special restrictions upon the enforceability of arbitration agreements, then, because the nature of such restrictions varies from state to state, life insurance companies could not enforce arbitration provisions in their policies unless they tailored those policies to conform to the requirements of individual states. Doing so would raise the cost of insurance. Moreover, because of the rather amorphous standards used in choice-of-law analysis, it is often difficult to predict which state's law might be applied to a particular policy. Consequently, in order to ensure that arbitration provisions in their policies will be enforced, life insurance companies would have to create policies that complied with the differing requirements of multiple states. To do so would be cumbersome at best and, in some cases, impossible.

ARGUMENT

I. MONTANA CODE ANN. § 27-5-114(4), WHICH CONDITIONS THE ENFORCEABILITY OF ARBITRATION PROVISIONS UPON STANDARDS THAT OTHER KINDS OF CONTRACTUAL PROVISIONS NEED NOT MEET, IS CONSEQUENTLY PREEMPTED BY SECTION 2 OF THE FEDERAL ARBITRATION ACT

A. Section 2 Of The Federal Arbitration Act Prevents States From Conditioning The Enforceability Of Arbitration Provisions Upon Standards That Other Kinds Of Contractual Provisions Need Not Meet

Section 2 provides that written agreements to arbitrate, when contained in a contract "evidencing a transaction involving [interstate] commerce," are "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added).[4] The Court has repeatedly held that Congress' intent in enacting this last phrase was to place arbitration agreements "upon the same footing as other contracts." *Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834, 838 (1995); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24, 33 (1991); *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 474, 478 (1989); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 225-226 (1987); *Dean Witter Reynolds v. Byrd*, 470 U.S. 213, 219 (1985); *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967) ("As the 'saving clause' in § 2 indicates, the purpose of Congress in 1925 was to make arbitration agreements as enforceable as other contracts . . . ."). Thus, state law may be applied to invalidate an arbitration provision only

[4] The same is true of separate agreements to arbitrate. *See* 9 U.S.C. § 2.

if the law "arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987).

It follows that if a state attempts to place arbitration provisions upon an unequal "footing" by requiring them to meet criteria that other kinds of contractual provisions need not meet, the additional requirements conflict with Section 2. *See Southland Corp.*, 465 U.S. at 16 n.11 (holding that a California statute that made arbitration agreements, but not other kinds of agreements, unenforceable was preempted by Section 2); *Perry*, 482 U.S. at 492 n.9 (finding that Section 2 preempted another California statute because "a state-law principle [of enforceability] that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with . . . § 2"). As this Court recently held in *Terminix:*

> What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The [Federal Arbitration] Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal "footing," directly contrary to the Act's language and Congress' intent.

115 S. Ct. at 843.

B. Mont. Code Ann. § 27-5-114(4) Conditions The Enforceability Of Arbitration Provisions Upon Standards That Other Kinds Of Contractual Provisions Need Not Meet, And Is Therefore Preempted By Section 2 Of The Federal Arbitration Act

Mont. Code Ann. § 27-5-114(4) ("the Montana notice statute") makes arbitration clauses unenforceable unless the contracts in which they appear contain a notice, "typed in underlined capital letters on the first page of the contract," that the contract is subject to arbitration.[5]

[5] Although the statute states that failure to comply with this requirement means that the contract "may" not be subject to arbi-

However, Montana law does not make the enforcement of other contractual provisions contingent upon the existence of such a notice. Consequently, the Montana notice statute does exactly what Section 2 forbids and is accordingly preempted as to all arbitration provisions that Congress has the power to regulate under Section 2.

In *Louisiana Public Service Commission v. FCC*, 476 U.S. 355, 369 (1986), the Court held that "[t]he critical question in any pre-emption analysis is always whether Congress intended that federal regulation supersede state law."[6] As discussed above in Part I.A. of the Argument, Congress clearly did intend Section 2 to supersede all state laws that create special obstacles to the enforcement of arbitration provisions. *See Perry*, 482 U.S. at 489 ("Section 2 . . . embodies a clear federal policy of requiring arbitration unless the agreement to arbitrate is not part of a contract evidencing interstate commerce or is revocable 'upon such grounds as exist at law or in equity for the revocation of any contract' ").

The Montana Supreme Court held that Section 2 does not preempt the Montana notice statute because the Montana statute "would not undermine the goals and policies of the FAA . . . ." Pet. App. 4a, 27a. But obviously the Montana notice statute *does* undermine what this Court has identified as the "basic purpose" of the Federal Arbitration Act: "to put arbitration provisions on 'the same footing' as a contract's other terms." *Terminix*, 115 S. Ct. at 840 (quoting *Scherk*, 417 U.S. at 511). The Montana Supreme Court's analysis, and its resulting conclusion that the Montana notice statute is not preempted, simply ignores (or at best misreads) both the plain language of Section 2 and the prior decisions of this Court.

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tration, the Montana Supreme Court has construed the statute to mean that the contract *shall* not be subject to arbitration. *See* Pet. App. 27a ("Because the agreement of the parties in this case did not comply with Montana's statutory notice requirement, it is not subject to arbitration, according to the law of Montana").

[6] Citing *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218 (1947).

II. PERMITTING STATES TO IMPOSE SPECIAL OBSTACLES TO THE ENFORCEMENT OF ARBITRATION AGREEMENTS WOULD INCREASE THE COST OF INSURANCE AND FORCE INSURERS TO COMPLY WITH REQUIREMENTS THAT NO SINGLE STATE WOULD HAVE IMPOSED

If states like Montana were allowed to flout Section 2 by placing special restrictions on the enforceability of arbitration agreements, life insurance companies could not enforce arbitration provisions in their policies unless they customized those policies to conform with the requirements of individual states, thus raising the cost of insurance. Moreover, because it is often difficult to predict which state's law might be applied to a particular policy, the only way for life insurance companies to guarantee that arbitration provisions in their policies will be enforced would be to create policies that complied with the special arbitration requirements of multiple states. However, it frequently would be difficult, if not impossible, to create such policies.

One way in which ACLI's members keep down the costs of their policies is to use nationally standardized forms. If it were necessary, in order to enforce a policy's arbitration provisions, that the policy be customized to comply with the special arbitration requirements of each state, such customizing would raise the costs of providing insurance and ultimately result in increased costs for policyholders. "[I]n insurance, as in other areas, customization invariably costs more than standardization." R. Keeton & A. Widiss, *Insurance Law* § 2.8, at 119 (1988).

Moreover, it is not always possible to predict which state's law will be applied when determining the enforceability of a particular policy's arbitration provisions. For example, even when a contract expressly specifies which state's law is to govern its enforcement, Montana will not apply that law if to do so would "violate[] Montana's public policy or [would be] against good morals." Pet. App. 17a (quoting *Youngblood v. American States Ins.*

Co., 866 P.2d 203, 205 (Mont. 1993)). Other states will also disregard the parties' choice of law on the basis of such considerations.[7] Obviously, it is difficult to predict when amorphous concepts like "public policy" or "good morals" might be used to invalidate the parties' choice of law.

Thus, if states were allowed to impose special restrictions on the enforcement of arbitration provisions, the only way to guarantee the enforcement of those provisions would be to issue policies that met the special arbitration requirements of all the states whose law might be applied. That could involve meeting the requirements of many states, because policyholders often move to another state after purchasing life insurance policies, it is obviously difficult to predict where they might move, and a court might apply the law of the new state in determining whether a policy's arbitration provision was enforceable. *See* Restatement (Second) of Conflict of Laws § 192 cmt. d (1988) (if the policyholder changes the state of his domicile after applying for a life insurance policy, a court might, in some cases, apply the law of the new state to issues arising under the policy). As a result, insurers would be required to contend with a cumbersome set of require-

[7] The Restatement (Second) of Conflict of Laws, which is followed by many states, provides that courts may refuse to enforce the parties' choice of law if, among other things, applying the law of the chosen state "would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which . . . would be the state of the applicable law in the absence of an effective choice of law by the parties." Restatement (Second) of Conflicts of Law § 187(2)(b) (1988). *See, e.g., Cherry, Bekaert & Holland v. Brown*, 582 So.2d 502, 507-508 (Ala. 1991) (refusing to enforce parties' choice of law); *National Glass, Inc. v. J.C. Penney Properties, Inc.*, 650 A.2d 246, 248-251 (Md. 1994) (same); *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 677-681 (Tex. 1990) (refusing to enforce parties' choice of law, but noting that the Restatement "offers little guidance" in determining what constitutes the "fundamental" policy of a state), *cert. denied*, 498 U.S. 1048 (1991).

ments, in the aggregate, that no individual state would have imposed. Furthermore, because those requirements often differ, and may even be inconsistent with each other, it would frequently be difficult, if not impossible, to comply with all of the potentially applicable requirements.[8]

CONCLUSION

For all of the foregoing reasons, the judgment below should be reversed.

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[8] An example of how states' requirements may differ is the variation in notice requirements for arbitration provisions. Montana and South Carolina require special notice of such provisions to be placed on the first page of contracts containing such provisions, while Missouri requires such notice to be placed adjacent to the signature block. S.C. Code Ann. § 15-48-10(a) (Law Co-op. Supp. 1995); Mo. Ann. Rev. Stat. § 435.460 (Vernon 1992). In addition, Rhode Island requires that arbitration provisions in insurance contracts must be placed immediately above the parties' signatures, whereas Iowa requires (in the case of tort claims) that the agreement to arbitrate must be in a separate writing executed by the parties. R.I. Gen. Laws § 10-3-2 (Supp. 1995); Iowa Code Ann. § 679A.1(2)(c) (West 1987). In order to comply with all of these statutes, a contract would have to contain special notices of arbitration both at the beginning and the end of the contract, and would have to contain arbitration agreements both in the body of the contract and in a separate writing. Compliance with these varying requirements would be cumbersome and inefficient, to say the least, and would involve surmounting a set of obstacles that none of these states would individually have imposed.